



HF 2527 – Tax Credit Reductions and Review (LSB 5795HV)
Analyst: Jeff Robinson (Phone: 515-281-4614) (jeff.robinson@legis.state.ia.us)
Fiscal Note Version – New

House File 2527:

- Creates a Legislative Tax Expenditure Committee of the Legislative Council and establishes the membership and duties of the Committee, including a five-year schedule for reviewing existing tax credits and the schedule starts in 2011.
- Reduces the annual limit on specific tax credit programs administered by the Department of Economic Development from the current \$185.0 million to \$120.0 million. The change is effective FY 2010.
- Suspends the Film Tax Credit Program by prohibiting the registration of new projects until July 1, 2012.
- Alters the Supplemental Research Activities Credit by increasing the current 6.5% maximum credit to 10.0% for companies with gross annual sales of less than \$20.0 million. For companies with higher gross annual sales, the tax credit is reduced from 6.5% to 3.0%. The change impacts only future awards.
- Lowers the annual cap for some tax credit programs and discontinues other tax credit programs. Impacted tax credit programs include:
 - Accelerated Career Education (ACE) Withholding Tax Credit
 - Agriculture Asset Transfer Tax Credit
 - Economic Development Region Revolving Loan Fund Tax Credit
 - Endow Iowa Tax Credit
 - School Tuition Organization Tax Credit
 - Iowa Fund of Funds Tax Credit
 - Venture Capital Investment Tax Credit
 - Value-added Agricultural Products Refundable Tax Credit
 - Historic Preservation and Cultural & Entertainment District Tax Credit
- Reenacts the Estate Tax to the extent a federal pick-up tax is allowed in the future.
- Requests that the Legislative Council establish 2010 interim committees to study the Enterprise Zone Program and the Industrial New Jobs Training Program (260E) with reports due to the General Assembly by January 15, 2011.

Assumptions

- Division II – Legislative Tax Expenditure Committee – The creation of a Legislative committee will have per diem and other minor administrative costs. It can also be assumed that although the Bill does not appropriate any funds for technical assistance to the Committee, the review work of the Committee will require significant staff time by the Departments of Revenue and Economic Development, as well as legislative staff. Additional reporting requirements may also be expected of other agencies and local governments. If the review identifies inefficient or ineffective tax preferences and those items are improved or ended, the review could substantially improve the economic efficacy of the State's overall tax incentive policy.
- Division III – Reduction in the Aggregate Annual Allowable Tax Credit Cap – The Bill reduces the current annual cap for three major Department of Economic Development

(DED) business subsidy programs, Enterprise Zones, High Quality Jobs, and Film Tax Credits. The current annual tax credit cap is \$185.0 million and the Bill reduces the cap to \$120.0 million effective FY 2010. With suspension of the Film Tax Credit program and given the present economic environment, it is assumed for this fiscal impact estimate that the lower cap will have no effect on tax credit awards in FY 2010 or FY 2011, but will reduce overall awards made in FY 2012 and for the foreseeable future by \$65.0 million per year. Since tax credit redemptions are spread over several years after they are awarded, the impact on net General Fund revenue in the initial years is projected to be low.

- Division IV – Suspension of the Film Tax Credit Program – This projection assumes that without Legislative action to suspend the Film Tax Credit program and/or lower the current \$185.0 million aggregate tax credit cap, the DED will begin to approve additional film projects in calendar year 2011. This projection further assumes that if a \$120.0 million aggregate cap is enacted, the DED will not resume approving film projects in the foreseeable future.
- Division V – Supplemental Research Activities Credit – The Bill enhances the supplemental credit for companies with annual gross sales under \$20.0 million and reduces the supplemental credit for companies with higher gross sales. The changes would not impact tax credit agreements already in place and there is often a lag between when a project is approved for the supplemental credit and when the credit is actually redeemed. Therefore, the impact on net General Fund revenue is expected to be low in the initial years.
- Division VI – Accelerated Career Education (ACE) Withholding Tax Credit – The maximum annual cap is reduced from \$6.0 million to \$5.4 million. The ACE program is currently not operating at its full \$6.0 million cap and the impact of the lower cap is calculated from projected usage, not from the current cap.
- Division VII – Agricultural Asset Transfer Tax Credit – The maximum annual cap is reduced from \$6.0 million to \$2.0 million. The program is currently not operating at its full \$6.0 million cap and the impact of the lower cap is calculated from projected usage, not from the current cap.
- Division VIII – Economic Development Region Revolving Loan Fund Tax Credit – The Bill repeals this tax credit.
- Division IX – Endow Iowa Tax Credit – The maximum annual cap is reduced from \$3.0 million to \$2.7 million.
- Division X – School Tuition Organization Tax Credit – The maximum annual cap is reduced from \$7.5 million to \$6.75 million.
- Division XI – Fund of Funds Tax Credit – This tax credit ensures that investors in the Fund of Funds will receive their entire investment back, along with an agreed to rate of return when their specified investment in the Fund of Funds is liquidated. If the returns received after the specified investment is liquidated are insufficient to cover the investment, contingent tax credits sufficient to make the investor whole are activated. Since the first investment is not scheduled to be liquidated for several years, the actual amount of tax contingent tax credits that will be necessary is not known. Without the language in the Bill, the maximum liability to the State General Fund is \$100.0 million, with a maximum annual redemption of \$20.0 million per year. With the language in the Bill, the maximum liability to the State General Fund is \$60.0 million, and the maximum annual redemption remains at \$20 million per year.
- Division XII – Venture Capital Investment Tax Credit – The Bill repeals this tax credit.
- Division XIII – Refundable Value-Added Agriculture Tax Credits – Iowa Code Section 15.333(3) allows certain projects approved under the High Quality Jobs Creation Act to receive a portion of their tax credits as refundable tax credits. The maximum annual amount of refundable credits the DED may approve is \$4.0 million. The \$4.0 million awarded by the DED is part of the aggregate tax credit cap (see Division III above). This fiscal estimate assumes that under current law, a sufficient volume of qualified projects will occur each year

to fully utilize the refundable \$4.0 million and the refunds will impact the State General Fund in the fiscal year following the award.

- Division XIV – Historic Preservation and Cultural & Entertainment District Tax Credit – The maximum annual amount of Historic Preservation Tax Credits that may be awarded for one tax year is reduced from \$50.0 million to \$45.0 million. The change first impacts FY 2013 and the first full year of impact is FY 2014. The tax credits are refundable so the impact of the lower credit limit is immediate.
- Division XV – Iowa Estate Tax Reenactment – Former federal estate tax law allowed states to impose a tax against an estate, with the dollar amount of the state tax reducing the federal estate tax due dollar-for-dollar. This was commonly referred to as the “pick-up tax”. The federal government rescinded the pick-up tax provision in the mid-2000’s as part of a total phase-out of the federal estate tax. The federal estate tax and the corresponding pick-up tax provision are scheduled to return after December 31, 2010. Should this occur, Division XV would allow the State of Iowa to receive revenue from the pick-up tax without increasing the overall tax on an estate.
- Divisions XVI and XVII – Interim Study Committees – Requests that the Legislative Council create two interim study committees, one to evaluate the Enterprise Zone Program and one to evaluate the Industrial New Jobs Training Program (260E).

Fiscal Impact

The following table provides the projected direct impact on net General Fund revenue associated with the tax credit changes contained in the Bill.

		Estimate of Reduction in Tax Credit Redemptions & Increase in Estate Pick-up Tax Collections - Net General Fund Revenue Increase by Fiscal Year (\$ in millions)			
Bill Division		FY 2011	FY 2012	FY 2013	FY 2014
III	Aggregate Cap at \$120.0 million	\$ 0.0	\$ 0.0	\$ 3.0	\$ 5.4
IV	Film Suspension	0.0	19.0	23.4	14.0
V	Research Activities	0.0	0.0	0.3	1.0
VI	Accelerated Career Education	0.4	0.4	0.4	0.4
VII	Agriculture Asset Transfer	0.4	0.9	1.6	2.3
VIII	Econ. Develop. Region	0.0	0.0	0.0	0.0
IX	Endow Iowa	0.1	0.2	0.2	0.2
X	School Tuition Organization	0.5	0.7	0.7	0.7
XI	Fund of Funds	0.0	0.0	0.0	0.0
XII	Venture Capital Investment	0.0	0.0	0.0	0.0
XIII	Value-added Ag Refundable	4.0	4.0	4.0	4.0
XIV	Historic Preservation	0.0	0.0	2.3	5.0
XV	Estate Pick-up Tax	0.0	28.5	46.2	46.9
		<u>\$ 5.4</u>	<u>\$ 53.7</u>	<u>\$ 82.1</u>	<u>\$ 79.9</u>

Longer term, the Bill lowers annual tax credit awards and redemptions by approximately \$75.7 million and increases potential annual estate tax revenue by \$47.0 million through reenactment of the estate pick-up tax. The Bill also lowers the potential program lifetime liability of the Fund of Funds Tax Credit by \$40.0 million, although that amount is not included in the table below.

Estimate of Reduction in Tax Credit Redemptions &
Increase in Estate Pick-up Tax Collections -
Net General Fund Revenue Increase
(\$ in millions)

	<u>Max Impact Per FY</u>
Aggregate Cap at \$120.0 million, Value-Added Ag Refundable, and Research Activities Credit Changes	\$ 65.0
Accelerated Career Education	0.6
Agriculture Asset Transfer	4.0
Endow Iowa	0.3
School Tuition Organization	0.8
Historic Preservation	5.0
Estate Pick-up Tax	<u>47.0</u>
	\$ 122.7

In addition, the Bill will require a projected \$200,000 to \$300,000 annually in State agency staff time (primarily the Departments of Revenue and Economic Development as well as the Legislative staff) to provide assistance to the Legislative Tax Expenditure Committee. The Bill does not provide funding so the expenditures are assumed to require the utilization of existing agency resources.

Sources

Department of Revenue
Legislative Services Agency Analysis

/s/ Holly M. Lyons

March 17, 2010

The fiscal note for this Bill was prepared pursuant to [Joint Rule 17](#). Data used in developing this fiscal note is available from the Fiscal Services Division of the Legislative Services Agency upon request.